

INTERIM REPORT NO. 1

REGARDING POSSIBLE ABUSE,

FRAUD, AND ILLEGAL ACTS BY

SAN DIEGO CITY OFFICIALS AND EMPLOYEES

REPORT OF THE

SAN DIEGO CITY ATTORNEY

MICHAEL J. AGUIRRE

OFFICE OF
THE CITY ATTORNEY
CITY OF SAN DIEGO

1200 THIRD AVENUE, SUITE 1620
SAN DIEGO, CALIFORNIA 92101-4178
TELEPHONE: (619) 236-6220

14 JANUARY 2005

I. PREDICATION OF CITY ATTORNEY INVESTIGATION

A. Investigation Related to 2003 Financial Statement Audit

The San Diego City Attorney is investigating possible abuse¹, fraud and illegal acts by San Diego City officials and employees. The scope of this investigation will extend to all possible illegal acts and will expand as necessary based on findings made during the investigation, in other words, the City Attorney's office will pursue all evidence of possible illegal acts no matter where they may lead.²

This investigation is predicated³ upon the request of the City of San Diego's outside auditor, KPMG LLM ("KPMG") based upon the following facts:

We understand that the SEC is conducting a formal investigation of the City of San Diego's public disclosures relating to the SDCERS⁴ in the City's bond offerings during the period 1996 through January 2004. This investigation was commenced following the City's filing of a Voluntary Report of Information on January 27, 2004, with the Municipal Securities Rulemaking Board and the Nationally Recognized Municipal Securities Information Repositories. That Voluntary Report made new disclosures regarding the City's obligations to fund the SDCERS and also disclosed that there had been errors in the City's 2002 CAFR [Comprehensive Annual Financial Report].

¹ Abuse "involves behavior that is deficient or improper when compared with behavior that a prudent person would consider reasonable and necessary business practice given the facts and circumstances." General Accounting Office, Government Auditing Standards 4.19.

² 11 October 2004 letter from Steven G. DeVetter to Les Girard, p. 8.

³ "Predication is the totality of circumstances that would lead a reasonable, professional trained, and prudent individual to believe a fraud has occurred, is occurring, or will occur. Predication is the basis upon which an examination is commenced." [2003 Association of Certified Fraud Examiners, Fraud Examiners Manual p. xxvii.]

⁴ "SDCERS" refers to the San Diego City Employees Retirement System.

We also understand that the U.S. Attorney and FBI are conducting a criminal investigation relating to the City's pension funding and disclosures. There have also been press reports of an additional investigation by the FBI relating to possible "public corruption" issues relating to the process by which the City and SDCERS have negotiated and approved various agreements in which the City's obligations to make payments to fund SDCERS were reduced and/or deferred in exchange for agreements to increase or expand benefits. [fn 1 "Potential illegal acts by SDCERS or its board are relevant to KPMG's audit. Your (City of San Diego) position (expressed in the September 20, 2004 letter), that SDCERS is an "entity independent of the City," does not address the fact that the financial condition of SDCERS is reported as a fiduciary fund in the City's CAFR."]

We understand that all of these investigations are focused on the conduct of individuals who either are currently employed by the City, were employed by the City during the period covered by KPMG's ongoing audit, or were acting in some manner on behalf of the City or SDCERS during the relevant time period.⁵

B. KPMG Concerns About Investigation by City's Outside Law Firm

The City of San Diego retained an outside law firm, Vinson & Elkins (V&E) to conduct an investigation into the underlying facts identified as the possible basis for finding fraud or that illegal acts had been committed.⁶ V&E was also retained to represent the City of San Diego in the Securities & Exchange Commission's ("SEC") investigation of City officials and employees.⁷ V&E issued its report on 16 September 2004.⁸

⁵ 11 October 2004 letter from KPMG partner Steven G. DeVetter to San Diego Assistant City Attorney Leslie J. Girard.

⁶ 18 February 2004 Retainer letter from Paul Maco to Casey Gwinn.

⁷ See fn 6, 18 February 2004 Retainer letter from Paul Maco to Casey Gwinn.

⁸ 16 September 2004 Report on Investigation The City of San Diego, California's Disclosures of Obligation to Fund the San Diego City Employees' Retirement System and

KPMG has determined that V&E's 16 September 2004 Report did not resolve key issues related to whether City of San Diego officials and employees engaged in illegal or fraudulent acts:

Unfortunately, based upon the information we have been provided to date regarding the scope and method of the V&E investigation, we do not believe the statement in the report that "it is difficult to attribute the City's failure to fully and accurately describe [pension] matter[s] to intentional misconduct on the part of individual employees" is sufficient to resolve the issue of potential illegal acts for purposes of KPMG's audit because it is not based on an investigation that had a scope and methodology that would provide a reliable basis for reaching a conclusion as to whether City officials engaged in intentional misconduct or other conduct, which violated any law, rule or regulation having the force of law.⁹ (Emphasis added)

On 29 October 2004 KPMG took the additional step of asking the City to hire a new outside law firm to continue with the investigation into possible fraudulent or illegal acts. KPMG reminded the City that the proper completion of the investigation was required if KPMG is to complete its audit of the City's financial statement:

If the City is prepared to proceed with an appropriate investigation, then we urge you to consider retaining counsel other than V&E to do so. The positions asserted in, and oppositional tone of, Mr. Maco's letter raises questions about V&E's willingness or ability in these circumstances to complete the investigation of, and reach conclusions on, the audit-critical questions posed in our prior oral and written communications and to do so in an objective and independent manner. Our reading of the letter suggests to us that, at this point, conducting the kind of investigation that is necessary may be in

Related Disclosure Practices 1996-2004.

⁹ See fn 2, 1 October 2004 letter from KPMG partner Steven G. DeVetter to San Diego Assistant City Attorney Leslie J. Girard, see also fn 10, 29 October 2004 letter from KPMG partner Steven G. DeVetter to San Diego City Mayor Dick Murphy and San Diego City Manager Lamont Ewell.

tension with V&E's ongoing representation of the City in the pending SEC investigation. KPMG's ability to complete its audit of the City's financial statements is dependent on resolution of these outstanding issues.¹⁰

KPMG reached its conclusions that the V&E 16 September 2004 Report was inadequate based upon the following analysis and observations about the 16 September 2004 Report. KPMG noted that V&E found “systemic failures in the City's financial reporting and disclosure processes related to the SDCERS pension plan.”¹¹ The report found that “as late as the fall of 2003 the City's Disclosure Counsel thought information was being withheld from him and there were fundamental disagreements about whether acknowledged errors in the historical financial statements were material.”¹²

KPMG further noted that the report acknowledges that the City's prior SDCERS related disclosures were inadequate, its disclosure system was dysfunctional and that the City had taken a “minimalist approach to public disclosure.”¹³ KPMG also found important the fact that “the City Auditor was disinclined to include information in the City disclosure that reflected badly on the City and would sometimes excise negative statements from disclosure documents.”¹⁴

¹⁰ 29 October 2004 letter from KPMG partner Steven G. DeVetter to San Diego City Mayor Dick Murphy and San Diego City Manager Lamont Ewell.

¹¹ See fn 2, 11 October 2004 letter from KPMG partner Steven G. DeVetter to San Diego Assistant City Attorney Leslie J. Girard citing to the 16 September 2004 Report pp. 170-171 which refers to “across the board failures of the City's internal disclosure processes.”

¹² See fn 2, 11 October 2004 letter from KPMG partner Steven G. DeVetter to San Diego Assistant City Attorney Leslie J. Girard citing to the 16 September 2004 Report pp. 114-120.

¹³ See fn 2, 11 October 2004 letter from KPMG partner Steven G. DeVetter to San Diego Assistant City Attorney Leslie J. Girard.

¹⁴ See fn 2, 11 October 2004 letter from KPMG partner Steven G. DeVetter to San Diego Assistant City Attorney Leslie J. Girard citing to the 16 September 2004 Report p. 117.

KPMG found telling the fact that both “the City and V&E have made it clear to KPMG that V&E was not retained to investigate issues relating to intent or whether any individual's conduct violated any law, rule or regulation, and that the scope of its investigative efforts were not designed to do so.”¹⁵

C. Investigation Required by KPMG

KPMG has made clear the nature of the investigation it requires to complete its audit of the City’s 2003 financial statements: “The report based on such an investigation must include clear conclusions and be supported by a thorough investigation.”¹⁶

In order to expeditiously address the issues raised by KPMG and avoid the necessity of retaining yet another law firm, the San Diego City Attorney’s Office has initiated an independent investigation into the possible abuse, fraud, and illegal acts of concern to KPMG.¹⁷ The City Attorney’s Office is working cooperatively with V&E and KPMG in order to complete the 2003 audit.

II. SAN DIEGO MAYOR’S BLUE RIBBON COMMITTEE ON CITY OF SAN DIEGO FINANCES¹⁸

A. COMMITTEE ESTABLISHED TO REPORT ON CITY OF SAN DIEGO FINANCES

At the beginning of his term in office, Mayor Dick Murphy announced he would convene a Mayor’s Blue Ribbon Committee on City of San Diego Finances to make an independent evaluation of the City's current fiscal health and make any

¹⁵ See fn 2, 11 October 2004 letter from KPMG partner Steven G. DeVetter to San Diego Assistant City Attorney Leslie J. Girard.

¹⁶ See fn 2, 11 October 2004 letter from KPMG partner Steven G. DeVetter to San Diego Assistant City Attorney Leslie J. Girard.

¹⁷ 9 December 2004 San Diego City Attorney news release announcing that the San Diego City Attorney was conducting an independent investigation into the matter.

¹⁸ Blue Ribbon Committee Report on City of San Diego Finances, Table of Contents, pp. 20-21.

appropriate recommendations. In April 2001 the Mayor announced the formation of the Mayor's Blue Ribbon Committee on City of San Diego Finances.

The Mayor emphasized in his news release announcing the formation of his Blue Ribbon Committee on City of San Diego Finances that the committee members are "all professionals in the community, not City employees." The Mayor's Blue Ribbon Committee on City of San Diego Finances mission, as set by the Mayor, was to:

- * Perform an independent evaluation of the fiscal health of the City of San Diego;
- * To review the budgeting principles of the City of San Diego;
- * Report the findings and recommendations to the City Council's Rules Committee.

B. MAYOR'S BLUE RIBBON COMMITTEE ON CITY OF SAN DIEGO FINANCES STAFFED BY AUDITOR

The Committee was staffed by former City Auditor Ed Ryan and current acting City Auditor Terri Aja Webster, the former Assistant City Auditor and Comptroller.¹⁹ The Committee was scheduled to issue its report to the City Council's Rules Committee in the Fall of 2001. However, the report by the Committee was not issued until February 2002.

C. MAYOR'S BLUE RIBBON COMMITTEE ON CITY FINANCES REPORT DID NOT DISCLOSE RISK OF PENSION TRIGGER

1. City Obligation to Make Multi-Million Dollar Balloon Payment

A substantial risk that the City would have to make a multi-million dollar balloon payment to the pension plan was not disclosed by Mayor's Blue Ribbon Committee on City of San Diego Finances. The City's obligation to make the

¹⁹ City of San Diego Mayor's Blue Ribbon Advisory Committee Announcement.

multi-million dollar balloon payment was created in 1996 by agreement between the Pension Board and the City. Under the agreement, known as Managers Proposal 1 (“MP 1”), the City agreed to make a balloon payment if the ratio of fund assets to liabilities fell below a “trigger” of 82.3% (“Pension Funding Trigger”):

The City will pay the agreed-to-rates shown above for FY 96 through FY 2007. In the event that the funded ratio of the System falls to a level 10% below the funded ratio calculated at the June 30, 1996 actuarial valuation [92.3%²⁰] which will include the impact of the benefit improvements included in this Proposal, the City-paid rate will be increased on July 1 of the year following the date of the actuarial valuation in which the shortfall in funded ratio is calculated. The increase in the City-paid rate will be the amount determined by the actuary necessary to restore a funded ratio no more than the level that is 10% below the funded ratio calculated at the June 30, 1996 actuarial valuation.²¹

2. Risk Pension Plan Funding Rate Falls Below Trigger

In October 2001 San Diego Assistant City Auditor Terri Webster²² grew fearful that pension fund losses would require the City to make the multi-million dollar balloon payment required by the Pension Funding Trigger contained in the MP1 agreement:

By late 2001, City officials began to fear that these plummeting returns were likely to pull SDCERS’ funded ratio below the 82.3% floor provision of MP 1. In an e-mail from Terri Webster to Deputy City Manager Cathy Lexin, dated October 11, 2001, and cogently titled “EEEEK,” Ms. Webster stated to her fellow SDCERS Board

²⁰ 16 September 2004 Report p. 45.

²¹ 23 July 1996 Cathy Lexin (City of San Diego Labor Relations Office) Memorandum re: City Manager’s Retirement Proposal.

²² Under § 144 of the San City Charter the City Auditor sits on the pension board. During 2002 Ms. Webster was the auditor representative on the pension board.

member:

YTD SDCERS earnings as of August 31, 2001 in the SDCERS Trust fund is about \$15m compared to \$53M same time 2000... a 71% drop! BEFORE 9-11-01! It will be tight to even meet the base undistributed earnings distributions for FY 02 (i.e., 13th Check, Corbett, etc.). I hope meet and confer negotiations result in returning as much of the \$100 million as possible to employer reserves because the Trust Fund really need[s] to build its equity and halt cost increases to ride through the next few years and keep a fiscally sound funding ratio (Underline added).²³

In February 2002 Assistant City Auditor Terri Webster learned from the 2001 fiscal year pension actuarial report that the pension's funding ratio had dropped to within 7.6% of the Pension Funding Trigger.²⁴ In other words Ms. Webster learned the City was facing the very real prospect of having to make the multi-million dollar balloon payment to the employee pension fund:

The concern that the trigger would be hit that year or the next year or the next increased substantially when a draft of the actuarial report for FY 2001 became available on February 12, 2002. The actuarial valuation for June 30, 2001 showed a funded ratio of 89.9%, a decline of approximately 8% [from \$68 million to \$283 million] over the previous year, not including the effects of the contingent of the Corbett settlement. Given the continued decline in the market that had occurred after June 30, 2001, it was apparent that a significant additional deterioration in SDCERS' funded ratio should be anticipated at the next valuation.²⁵

²³ 16 September 2004 Report p. 79.

²⁴ Ms. Sally Zumwalt, former pension plan administrator, explained in a statement given on 11 January 2004 that it was her practice to distribute to Ms. Webster pension board materials. Ms. Zumwalt stated that she took the board documents directly to Ms. Webster's office. Ms. Zumwalt had previously worked for the City Auditor's office.

²⁵ See fn 23, 16 September 2004 Report p. 79.

The EEEK memorandum illustrated that Ms. Webster knew the City pension had suffered a 71% drop in its investment earnings in the first two months following the end of the 2001 fiscal year. Eight months of losses suffered by the pension plan in fiscal 2002 pushed the plan's funding ratio even closer to the trigger point. Despite this information, in February the Mayor's Blue Ribbon Committee on City of San Diego Finances issued its report showing the funding ratio to be 97%. The Pension Funding Trigger was eventually hit "as of the Fund's June 30, 2002 actuarial valuation."²⁶ As set forth below, the City would have needed more than \$500 million to make the balloon payment to the pension plan.²⁷

The City Auditor had a duty to know about and bring the threat of the Pension Fund Trigger to the attention of the Mayor, Manager and Council. Amongst the "core" financial accounting services the San Diego City Auditor has a duty to:

"Analyze the annual actuary report and make projections of the fiscal impact of contributions as needed. Calculate City contribution rates using information provided on the actuary report and advance to Retirement Fund."²⁸

Moreover, the City Auditor was expressly required to inform the Mayor, Council and Manager of these facts. The City Auditor:

[S]hall submit to the City Manager and to the Council at least monthly a summary statement of revenues and expenses for the preceding accounting period, detailed as to appropriations and funds in such manner to show the exact financial condition of the City and each Department, Division and office thereof.²⁹

²⁶ 5 February 2003 Pension Plan Response to Blue Ribbon Report on City Finances.

²⁷ See fn 23, 16 September 2004 Report p. 79.

²⁸ 26 December 2000 memorandum from Ed Ryan to SDCERS Board of Administration.

²⁹ San Diego City Charter § 39

Thus, by February 2002 City officials should have been well aware that a probable decline in the funding ratio of the pension plan created the real prospect that the City would have to make a multi-million balloon payment to raise the pension plan's funding ratio above the established level of 82.3%. Outside counsel Paul Maco found that if the Pension Funding Trigger was reached that by "rough estimate, the City would have needed to pay more than \$500 million in FY 2004 and 2005 to restore the funded level to 82.3%."³⁰

3. Mayor's Blue Ribbon Committee Report on City of San Diego Finances Falsely States Funding Ratio

The Mayor's Blue Ribbon Committee on City of San Diego Finances publicly presented its report to the Rules Committee of the San Diego City Council on 27 February 2002.³¹ The Mayor's Blue Ribbon Committee Report on City of San Diego Finances represented to the Rules Committee and the public that the City's employees pension was "currently funded at 97% (i.e. its current assets equaled 97% of the actuarially computed present value of the future Pension Plan liabilities)."

The Mayor's Blue Ribbon Committee Report on City of San Diego Finances report stated as follows:

C. FUNDING LEVEL

SDCERS is not in a fully funded position. It is currently funded at 97% (i.e. its current assets equaled 97% of the actuarially computed present value of the future Pension Plan liabilities). The absolute dollar amount of under funding hit a peak of \$148 million in Fiscal Year 1999. Excellent Pension asset investment performance reduced that unfunded liability to \$69 million in Fiscal Year 2000. However, investment performance in Fiscal Year 2001 was less than half of the excellent performance in Fiscal Year 2000. Investment performance in the first seven months of Fiscal Year 2002 is lower than in Fiscal

³⁰ See fn 23, 16 September 2004 Report p. 79.

³¹ 27 February 2002 Meeting Minutes of the Committee on Rules, Finance, and Intergovernmental Relations. At this time, the Rules Committee was chaired by Mayor Dick Murphy, and staffed by City Councilpersons Wear, Madaffer, Stevens, and Atkins.

Year 2001. It is expected that the forthcoming actuarial report will show an increase in the unfunded dollar amount.

**San Diego City Employees' Retirement System Financial Information
For Fiscal Years 1996 - 2001
(\$ IN MILLIONS)**

	2001	2000	1999	1998	1997	1996
Pension Fund Assets	\$2,807	\$2,999	\$2,476	\$2,272	\$1,855	\$1,604
City Pension Expense	\$68	\$61	\$56	\$51	\$48	\$44
Pension Plan & Health Benefits Paid	\$155 ¹	\$112	\$100	\$85	\$67	\$62
Unfunded Actuarial Accrued Liability	Not available	\$69	\$148	\$125	\$117	\$140
Retiree Health Benefits Expense	\$7	\$5	\$5	\$4	\$5	\$5

¹ includes \$24 million Corbett pay out settlement. (Emphasis added)

The Mayor's Blue Ribbon Committee Report on City of San Diego Finances table contained an additional false statement that the fiscal year 2001 funding ratio was "Not available" when in fact it had been available 15 days earlier.³² Moreover, the Mayor's Blue Ribbon Committee Report on City of San Diego Finances was presented without correction to the City Council on 15 April 2002.³³

On 27 February 2002 the Rules Committee directed the City Manager to prepare a response to the report. Specifically, the Manager was asked to respond to any aspects of the report dealing with the pension fund. Staff was instructed to return to the Committee on 20 March 2002. On that date, the City Manager

³² Fiscal year 2001 pension plan actuarial report.

³³ Minutes for the 27 February 2002, 20 March 2002 Rules Committee and the 15 April 2002 City Council Meeting.

returned to the Committee with his response. Despite the updated investment returns and the new Annual Actuarial Valuation for FY 2001, no amendments, changes, disclaimers or caveats were made to the 97% figure that was presented on 27 February 2002.³⁴ In fact, at the close of the report, the Mayor remarked:

You will recall that the numbers here in the report show that we're funding somewhere between . . . in excess of 90% of the needs of the system. But 100% would be the ideal way to operate.³⁵

On 15 April 2002, the Mayor's Blue Ribbon Committee on City of San Diego Finances presented its report to the entire City Council. At that time, the Council was informed that the pension plan's funded ratio was 97%, which represented an unfunded liability of \$68.95 million. Again, no disclaimers or modifications were made to that figure. This was a false statement of fact. As stated, the Annual Actuarial Valuation released on 12 February 2002, stated that the employee pension plan was actually funded at 89.9%, which represented a significantly higher unfunded liability of \$283.89 million.

Even though the SDCERS actuarial report for June 2001 showing the City's pension plan funding ratio had dropped was already available it was not disclosed in the Mayor's Blue Ribbon Committee Report on City of San Diego Finances. Further, Ms. Webster's EEEK memorandum citing a precipitous drop in the value of the Pension Plan's investment portfolio following the June 2001 valuation was also not disclosed in the Mayor's Blue Ribbon Committee Report on City of San Diego Finances.

One week before the Mayor's Blue Ribbon Committee Report on City of San Diego Finances was presented to the City Council, the San Diego Union Tribune reported that the pension plan had lost money the prior year. There was no mention of the fact that the pension plan was on its way to a 77.3% funding

³⁴ Memorandum from Dan Andrews, City Attorney Investigator who reviewed the contents of the audio tapes of the Rules Committee Meetings for 27 February 2002 and 20 March 2002.

³⁵ Ibid. The City Attorney's Office is currently investigating whether, as of 20 March 2002, the Mayor had prior knowledge of the actual funded ratio for the pension plan.

ratio which was 5% below the trigger. There was no mention of the trigger or the massive balloon payment the City would have to make into the system. Moreover, members of the Mayor's Blue Ribbon Committee on City of San Diego finances were cited in the article:

Members of a citizens committee on city finances, which raised questions in a recent report about city funding of the retirement system, agreed that the fund is sound and that retirees and current workers have nothing to fear. [5 April 2002 San Diego Union Tribune Article "Pension Fund lost millions last year/Unions say city retirees are in no financial peril]

The Mayor's Blue Ribbon Committee Report on City of San Diego Finances was not updated even after this article to reflect the fact that the City pension plan funding ratio had dropped to 89.9%. It was also not updated to show that the funding ratio trend line was headed to a point below the Pension Funding Trigger. The Mayor's Blue Ribbon Committee Report on City of San Diego Finances was not amended to reflect Ms. Webster's conclusion that it would be "tight even to meet the base undistributed earnings."³⁶

With the Mayor's Blue Ribbon Committee Report on City of San Diego Finances concealing the facts showing a massive financial tidal wave heading towards the City, City officials were left free to add hundreds of millions in new unfunded benefits to the pension plan deficit. First, City officials plotted to remove the Pension Funding Trigger. Second, City officials agreed in secret to add hundreds of millions of dollars in new unfunded benefits. City officials accomplished these two goals by renegotiating the Manager's Proposal I to avoid the "trigger." This initiative, entitled Manager's Proposal II, was adopted by the Retirement Board on 11 July 2002.³⁷ At roughly the same time, the City Council adopted a series of retirement benefit increases. These enhancements included an increase in the retirement factor for general members from 2.25% to 2.5%, the

³⁶ On 15 April 2002, following the Mayor's Blue Ribbon Committee Report on City of San Diego Finances, Council woman Frye made a motion directing the City Manager to return to the Council with a full report responding to the report of the Mayor's Blue Ribbon Committee on City of San Diego Finances. See fn 33.

³⁷ 16 September 2004 Report, p. 89.

establishment of the presidential benefit for union presidents, and the waiver of the 90% cap for select employees, including Ms. Webster.³⁸

By the fall of 2002 it became clear that the negative financial forecasts had materialized. On 16 September 2002, Terri Webster informed Retirement Administrator Larry Grissom that there were insufficient investment earnings to make the mandatory distributions required by the Municipal Code. Specifically, the investment earnings fell \$38 million short of the mark required to make the mandatory distributions.³⁹ On 26 December 2002 the actuarial report for FY 2002 was made available. The report indicates that as of 30 June 2002, the funded ratio of the plan had fallen to 77.3%, which represented an unfunded liability of \$720.7 million.⁴⁰ On 5 February 2003, SDCERS appeared at Rules to respond to the Blue Ribbon Committee. In that report, SDCERS observed that the “trigger event has occurred as of the Fund’s 30 June 2002 valuation.”⁴¹

III. CONCLUSION

Despite the substantial financial crisis faced by the City due to funding problems in the City pension plan the Mayor’s Blue Ribbon Committee Report on City of San Diego Finances represented the funding ratio as being 97%. Thus, the Mayor’s Blue Ribbon Committee Report on City of San Diego Finances contained a material false statement that the San Diego City Pension Plan’s funding ratio was 97% when in fact it was 89.9% funded as of 30 June 2001. The report also failed to disclose that by 11 October 2001 the audit staff of the City had determined that the investment portfolio of the City’s pension plan had dropped significantly. Finally, the possible triggering of the City’s duty to make a sizeable balloon payment to the plan was not mentioned. City officials allowed this misinformation to be perpetuated despite various opportunities to correct the record. Thus, taxpayers and other users of the Mayor’s Blue Ribbon Committee Report on City of San Diego Finances were misinformed about material financial information

³⁸ 16 September 2004 Report, p. 80.

³⁹ 16 September 2002 memorandum from Terri Webster to Larry Grissom.

⁴⁰ SDCERS Annual Actuarial Valuation 30 June 2002.

⁴¹ See fn 26, SDCERS response to the Mayor’s Blue Ribbon Committee Report on City of San Diego Finances, 5 February 2003.

regarding the City finances.

The failure to include accurate information about the dire financial condition of the City's employee pension plan in the Mayor's Blue Ribbon Committee Report on City of San Diego Finances used in February 2002 raises serious questions of misconduct by City officials. The City Attorney's office is now conducting an investigation to identify the parties responsible for putting the false material statement in the Mayor's Blue Ribbon Committee Report on City of San Diego Finances and allowing this misinformation and/or omitted facts to be disseminated to the Council, the market, and the public.

Had the public known that the City faced the very real prospect of having to pay hundreds of millions of dollars into the pension plan in order to meet its contractual duties under the MP1 agreement, would the City have proceeded with its decision to increase employee pension benefits by hundreds of millions of dollars? Had this information been disclosed would the City have continued to sell municipal bonds that did not make needed disclosures about the City's pension funding problems? Had this information been disclosed would the City be facing investigations by the SEC, FBI and US Attorney?

The second interim report will identify those City officials and employees responsible for the false statements and omitted material facts identified in this report. In addition, later interim reports will focus on additional abusive, illegal or fraudulent acts and the parties responsible for their commission.

MICHAEL J. AGUIRRE, City Attorney

By

Michael J. Aguirre
City Attorney